Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matters of	
Federal-State Joint Board on Universal Service	CC Docket No. 96-45
1998 Biennial Regulatory Review—Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms	CC Docket No. 98-171
Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990	CC Docket No. 90-571
Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size	CC Docket No. 92-237 NSD File No. L-00-72
Number Resource Optimization	CC Docket No. 99-200
Telephone Number Portability	CC Docket No. 95-116
Truth-in-Billing and Billing Format	CC Docket No. 98-170

REPLY COMMENTS OF
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As a leading provider of advanced Internet protocol ("IP") services to end users, Cable & Wireless USA, Inc. ("C&W") strongly supports the adoption of a universal service funding ("USF") mechanism based on the number and capacity of connections provided to a public network, as embodied in the proposal by the Coalition for Sustainable Universal Service ("CoSUS"). USF assessment mechanisms in the United States are particularly complex given the federal-state jurisdictional divide. This divide, coupled with recent market trends and technological shifts, has rendered the existing USF system unworkable. The CoSUS proposal—made in response to the Commission's Further Notice of Proposed Rulemaking in the above-captioned proceedings[1]—would remedy the deficiencies of the existing USF system in the most efficient and least discriminatory manner. In adopting such a proposal, however, the Commission must provide—as the CoSUS proposal would—for a reasonable transition period to allow carriers to adapt their financial and systems operations to the new regime.

With its affiliates, C&W is a major global telecommunications business with annual revenues of more than US $11 billion (as of March 2001) and customers in 70 countries. C&W's focus for future growth is on Internet protocol and data services and

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1 *See In re Federal-State Joint Board on Universal Service; 1998 Biennial Regulatory Review—Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms; Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990; Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size; Number Resource Optimization; Telephone Number Portability; Truth-in-Billing and Billing Format*, Further Notice of Proposed Rulemaking & Report & Order, CC Docket Nos. 96-45, 98-171, 90-571, 92-237, 99-200, 95-116, 98-170, NSD File No. L-00-72, FCC 02-43 (rel. Feb. 26, 2002) ("FNPRM").

solutions for business customers. C&W is currently developing advanced IP networks and value-added services in the United States, Europe, and the Asia-Pacific region in support of this strategy. With the capability of its global IP infrastructure and its strength in key markets, C&W holds a unique position in terms of global coverage and services to business customers.

C&W's reply comments are organized into four parts. *First*, C&W describes that the existing USF system is flawed because it depends on a shrinking revenue base and discriminates against interexchange carriers ("IXCs"). *Second*, C&W argues that a connection-based USF system, embodied in the CoSUS proposal, would provide stable USF funding without discriminating against particular classes of carriers or services and without imposing needless compliance burdens on carriers—particularly providers of advanced and IP-based services. *Third*, C&W argues that to achieve a smooth transition to a connection-based USF system, the Commission must provide for a reasonable transition period of at least one year. *Finally*, C&W argues that the Commission should continue to permit carriers to recover the administrative costs imposed by collection and remittance of USF-related assessments.

I. The Record Demonstrates that the Existing Revenue-Based USF System Is Flawed

The existing revenue-based USF system is flawed because it depends on a revenue base that is shrinking—a phenomenon which current market trends and technological shifts only reinforce. Moreover, this system generates costly market distortions and inefficiencies as it is particularly ill-suited to the offering of advanced services.

A. The Existing USF System Depends on, Yet Discriminates Against, Businesses with Declining Market Share and Revenues, Namely IXCs

The existing USF system is unsustainable as it relies on, yet discriminates against, businesses with declining market share and revenues, namely IXCs. The record amply demonstrates that the decline in IXC revenues is continuing, if not accelerating, even as USF grows.[2] In C&W's own experience, its own end-user interstate and international telecommunications services revenues have fallen over 30 percent over the past to years. But under the current USF system, these declining IXC revenues are offset by higher IXC contribution factors.[3] These higher contribution factors only encourage carriers to reclassify services so that they fall outside of the USF revenue base (to the extent they have such discretion). And the higher retail prices (caused by higher contribution factors) only encourages consumers to substitute services outside of the USF revenue base.

For example, in the 2000-2001 period, with falling end-user interstate and international telecommunications services revenues, C&W has been forced to cover its USF contributions either by raising its USF recovery charges or raising the prices it

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[2] *See, e.g.*, CoSUS FNPRM Comments at 21 (noting a 17-percent decline in per-quarter assessable end-user interstate and international IXC revenues from 1999 to the third quarter of 2001) and 21-22 (noting that wireline long-distance voice revenues declined 7.7 percent in 2000 and 11.6 percent in 2001); FNPRM ¶ 7 n.12 (noting declines in consumer services revenues of AT&T, WorldCom, and Sprint). Regarding USF growth, *see* Office of Management & Budget, Executive Office of the President, Budget for Fiscal Year 2003, Analytical Perspectives at 336 (2002) (noting that USF outlays in FY 2001 exceeded $4.9 billion and predicting that USF outlays will exceed $6.5 billion in FY 2003 and $7.11 billion in FY 2007).

[3] *See* Declaration of Daniel Kelley & David Nugent ("Kelley/Nugent Declaration"), Attachment 4 to CoSUS FNPRM Comments, at ¶ 7 (predicting that the contribution factor for interstate end-user revenues will increase from its current level of 7.8 percent to more than 10 percent by 2006).

charges for its services. In either case, C&W is put at a competitive disadvantage vis-à-vis interstate service providers who are not similarly burdened by falling revenues.

As recognized by the Commission and confirmed in the record, a number of market trends and technological shifts have contributed to the decline in IXC market share and revenues. *First*, IXCs have lost market share to regional Bell operating companies ("RBOCs") that have entered the in-region interLATA markets.[4] *Second*, IXCs have lost market share to wireless carriers, who have increasingly offered nationwide calling plans without roaming or other distance-based charges.[5] *Third*, IXCs have lost market share to providers of services which are not subject to universal service charges.[6]

Incentives in the existing USF system only reinforce and encourage the decline in IXC revenues, and consequently the USF revenue base. Carriers have an incentive to avoid USF assessments by bundling their interstate and international telecommunications services with intrastate telecommunications services, information services, and customer premises equipment.[7] And unlike incumbent local exchange carriers that have not been granted pricing flexibility (and which are subject to jurisdictional separation requirements), competitive local exchange carriers, which have flexibility in pricing have

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4 *See* Kelley/Nugent Declaration at ¶ 13 (noting loss in IXC market share); FNPRM ¶ 9 (noting RBOC market entry approvals and gains in respective market shares).

5 *See* Sprint FNPRM Comments at 2; Kelly/Nugent Declaration at ¶ 17, citing *In re Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993 Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Radio Services*, Sixth Report, 16 FCC Rcd 13,350, 13,382-83 (2001); FNPRM ¶¶ 11-12.

the discretion to classify certain revenues as intrastate rather than interstate, at least on a contract basis.[8] As revenues are classified as intrastate or non-telecommunications, they are removed from the USF assessment base. This declining USF assessment base necessitates a higher contribution factor, which only reinforces the carriers' incentive to bundle services so as to avoid the assessment.

Some critics of the CoSUS proposal have suggested that IXCs are seeking only to rid themselves of USF contribution obligations.[9] As C&W's experience indicates, however, this is far from the truth. Of C&W's current contribution base, roughly 80 percent is generated through provision of services to customers with dedicated lines. Adoption of the CoSUS proposal would in no way relieve C&W of its USF contribution obligations for these services.

B. When Applied to Advanced IP-Based Services, the Existing System Generates Costly Market Distortions and Inefficiencies

For providers of advanced services to end users in the United States, the existing revenue-based USF system imposes particular administrative burdens and encourages distortions. Such providers must evaluate each service, or package of services, offered to each of its customers to (1) characterize the service as telecommunications or non-telecommunications and then (2) determine the jurisdictional USF treatment for any end-user telecommunications service and its associated revenues. These exercises are costly

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7 *See* C&W NPRM Comments, CC Docket No. 96-45, at 5 (filed July 9, 2001); CoSUS FNPRM Comments at 23-25; FNPRM ¶¶ 12-13.

8 *See* 47 C.F.R. §§ 36.601 *et seq.* (setting forth jurisdictional separation requirements); C&W NPRM Comments at 4; SBC Comments at 11-12; CoSUS FNPRM Comments at 26.

9 *See, e.g.*, SBC FNPRM Comments, at 18.

and time-consuming for providers. By comparison, a connection-based approach would require a far simpler evaluation of the connection and capacity provided, without regard to the particulars of the services transmitted over the connection or the packaging or bundling of those services with other products or services. And it would eliminate the competition among carriers as to which carrier can develop the most creative structure that avoids federal universal service assessments.

II. The Commission Should Adopt a Connection-Based USF System Based on the CoSUS Proposal

C&W urges the Commission to adopt CoSUS's connection-based USF proposal.[10] The CoSUS proposal remedies all of the shortcomings of the existing revenue-based USF system, as outlined in part I above. And alone among the connection-based proposals presented to the Commission, the CoSUS proposal satisfies the requirement of Section 254(d) that any USF system be "equitable and nondiscriminatory."

A. The CoSUS Proposal Avoids Shortcomings of a Revenue-Based USF System

The CoSUS proposal would replace the existing revenue-based USF system, which is competitively distorted, inefficient, and dependent on a shrinking revenue base, and replace it with a stable and competitively- and technologically-neutral USF system with a growing revenue base.

[10] As noted in C&W's earlier comments on the NPRM, C&W takes this position in the United States based on the uniqueness and complexity of the U.S. regulatory situation, namely the interstate-intrastate jurisdictional divide. In countries with far simpler (and unitary) regulatory regimes, C&W continues to support a revenue-based approach. In all jurisdictions, however, C&W continues to favor USF contributions based on contemporaneous, rather than historical or forecasted, data. *See* C&W NPRM Comments at 7.

Under the CoSUS proposal, every interstate telecommunications carrier—whether wireline or mobile wireless—would be subject to USF obligations, and would contribute based on connections provided from a public network directly to retail customers (with mobile wireless carriers contributing based on the number of activated handsets in service).[11] The CoSUS proposal would thus eliminate the incentive and ability of carriers to bundle or classify services so as to avoid USF assessments. It would also eliminate the current USF system's blatant discrimination in favor of wireless carriers.[12]

Under the CoSUS proposal, private carriers that provide stand-alone interstate and international telecommunications connections to a public network for a fee to third parties would contribute, subject to certain exemptions in Part 54 of the Commission's rules.[13] The CoSUS proposal would thus ensure that any consumer shift away from POTS to advanced services would not undermine the USF revenue base, as those services also depend in large part upon connections between retail users and the public network.

By adopting the CoSUS proposal, the Commission would also eliminate the "contribution lag" generated by the existing USF system, in which assessments are based on gross revenues for interstate and international telecommunications services in the penultimate quarter before the assessment calculation is made. As C&W has noted previously, this contribution lag favors carriers with growing interstate and international revenues, as the USF assessment costs are incurred six months after the revenues on

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11 *See* CoSUS FNPRM Comments at 10.

12 *See also* C&W NPRM Comments at 6.

13 *See id.*

which the assessment is based are recognized.[14] This lag allows these carriers to spread the cost of their USF contributions across a larger revenue based by the time the contributions are in fact due.[15] But unlike some other proposals made to the Commission,[16] the CoSUS proposal would do more than tinker with the existing system to remedy the contribution lag, and instead remedy the fundamental flaws of the existing USF system, namely reliance on, and discrimination against, shrinking IXC revenues.

As most commenters agreed, a connection-based USF system also eliminates the need to impose a surcharge on customers to account for uncollectibles.[17] Under the current revenue-based USF system, carriers are given broad flexibility to charge for uncollected fees because they bear all the risk. USAC charges a given contribution factor set to cover a requirement level regardless of how likely customers are to pay USF fees. It is up to the carrier to estimate the level of uncollectibles and charge over and above the USAC charge.

Finally, the capacity-tiering provisions of the CoSUS proposal resolve the issue of how to reconcile high-capacity lines (which do not equate with a given number of PSTN lines) within a connection-based USF system.[18] As C&W has stated previously, the

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14 *See* C&W Comments at 7.

15 *See id.*; CoSUS FNPRM Comments at 29; SBC NPRM Comments at 5-6 (noting SBC's under-recovery of USF contributions due to contribution calculations based on historical data).

16 *See, e.g.*, Verizon FNPRM Comments at 4 (advocating a collect-and-remit approach under the existing revenue-based USF system); APCIC Comments at 11-12 (proposing a "projected cost" basis in place of historical data).

17 *See* WorldCom FNPRM Comments at 8; Verizon FNPRM Comments at 5; Sprint FNPRM Comments at 16; AT&T FNPRM Comments at 4.

18 *See* CoSUS FNPRM Comments at 13-14 and Attachment 1, at 2-3.

treatment of high-capacity lines in a connection-based USF system must be competitively neutral and must not discourage broadband deployment.[19] The CoSUS proposal satisfies these requirements.

B. The CoSUS Proposal Is Better Suited to Advanced and IP-Based Services

In proposing a connection-based USF system, the CoSUS proposal would better serve advanced services than would the existing revenue-based USF system. For C&W—a carrier focused on providing advanced services—this advantage is one of critical importance.

As a matter of technology, providers of advanced services do not draw sharp distinctions between telecommunications and information services. The transport layer of advanced networks is capable of hosting a variety of applications—some similar to telecommunications services, some dissimilar, and the vast majority include some computer processing or protocol conversion that characterizes an information service. Moreover, in the applications layer, the voice application is often integrated with other applications to offer customers a range of innovative enhancements far beyond a simple voice connection. Yet under the existing USF assessment mechanisms, carriers must attempt to assign a regulatory classification to these services in order to determine the appropriate USF treatments, potentially subject to some "second guessing" by the regulator at some later date.

The Commission should seek to limit the regulatory uncertainty, which only encourages more creative efforts by providers to classify service revenues out of the USF

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[19] *See* C&W NPRM Comments at 6-7.

contribution base and would stifle the development and deployment of advanced and IP-based services.[20] Instead, the Commission should adopt the CoSUS connection-based USF proposal both for its simplicity and technological neutrality. By focusing on the transport layer only, a connection-based USF system dispenses with the need for complex and burdensome categorization of applications.

C. Of the Connection-Based USF Proposals, Only the CoSUS Proposal Satisfies the "Equitable and Nondiscriminatory" Requirements of Section 254(d)

Of the connection-based USF proposals, only the CoSUS proposal satisfies the "equitable and nondiscriminatory" requirements of the Section 254(d) of the Communications Act of 1934, as amended. The other proposals proffered to the Commission suffer from some of the same defects as the existing revenue-based USF system by preserving discriminatory and inefficient aspects of the existing system.

The Sprint proposal to preserve the "interim" wireless safe harbor would explicitly discriminate in favor of mobile wireless carriers, and against both wireline IXCs and LECs.[21] As CoSUS has demonstrated, the shifting of 100 interstate calling minutes from a wireline IXC to a mobile wireless carrier reduces the universal service

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[20] *See* Level 3 Communications, Inc., NPRM Reply Comments, CC Docket No. 96-45 (filed July 9, 2001) (cautioning that the Commission "must resist the urge to capture IP-based services in the current regime by applying legacy regulatory classifications to characterize such services as telecommunications services, notwithstanding their use of net protocol conversion, access to stored databases, or computer processing").

[21] *See* Sprint Corporation NPRM Comments, CC Docket No. 96-45, at 8-9 and Attachment A (filed June 25, 2001) (proposing a connection-based methodology that would maintain current contribution ratio between wireline and mobile wireless carriers, including the 15-percent safe harbor factor for mobile wireless carriers); ; Sprint FNPRM Comments at 11-12 (same).

contribution amount by 80 percent.[22] And as noted in data from the Commission and the mobile wireless carriers themselves, the average per-month, per-connection USF recovery charge is $0.51 for an ILEC, whereas the average per-month, per-connection USF assessment for a mobile wireless carrier is $0.46.[23] Such discrimination is clearly inconsistent with the meaning of Section 254(d).

The SBC/BellSouth and NRTA/OPASTCO proposals would discriminate in favor of particular network architectures and disfavor long-distance providers who are not affiliated with access providers. Under these proposals, each end-user connection and each end-user customer relationship with an interstate transmission link provider would be assessed.[24] The SBC/BellSouth proposal would also base each of those assessments on the capacity of the connection.[25] Under either proposal, if an end user purchased a tariffed channel termination from an incumbent LEC and transport between the channel termination and an IXC POP from a CLEC, the architecture would generate two USF contributions. By comparison, if the end user purchased an incumbent LEC special access service, the architecture would generate only one USF contribution. The SBC/BellSouth and NRTA/OPASTCO proposals would also discriminate against IXCs by making them dependent on access providers for connection-related data—an arrangement that would give rise to the same data-lag problems that plague the existing

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22 *See* Kelley/Nugent Declaration at 10-11.

23 *See* FNPRM at ¶ 59; Sprint FNPRM Comments at 14; Voicestream FNPRM Comments at 2.

24 *See* SBC FNPRM Comments at 10; NRTA/OPASTCO FNPRM Comments at 12.

25 *See* SBC FNPRM Comments at 10-11.

revenue-based, historical-data-dependent USF system. The resulting discrimination is likewise inconsistent with Section 254(d).

III. To Implement a Connection-Based USF System, Carriers Will Need a Reasonable Transition Period of at Least One Year

To implement a connection-based USF system with a minimum of disruptions to carrier operations, the Commission should adopt a reasonable transition period of at least one year.

The CoSUS proposal addresses C&W's concerns about transitioning from the current revenue-based USF system to a connection-based USF system. Under that proposal—a hybrid, as it would treat certain lines differently during the transition period—the Commission would move immediately (*i.e.*, in July 2002) to a connection-based system for switched access lines and mobile wireless handsets serving residential, single-line business, and CMRS subscribers.[26] Providers of multiline business and special access/private line services, however, would for one year continue to pay universal service contributions based on the last previously established revenue-based contribution factor, which could rise or fall with other assessments during that year.[27] This one-year transition period would allow providers to develop systems to track and bill connection- and capacity-based charges and to make related budgeting and finance adjustments. At the end of the one-year transition period (roughly July 2003),

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[26] *See* CoSUS FNPRM Comments at 12.

[27] *See id.* at 12-13.

assessments for switched multiline business, special access, and private line services would be based on capacity charges, tiered by capacity amount.[28]

In the alternative, and particularly if the CoSUS "hybrid" proposal cannot be implemented immediately (as of July 2002), the Commission could move immediately to a collect-and-remit system (under the existing revenue-based approach) for all lines and services during the transition period and then move all lines and services to a connection-based USF system at the end of the transition period. All providers are prepared to make an immediate switch to a collect-and-remit system during the transition period, as their operations and budgeting processes are already established for a revenue-based USF system. By moving to a collect-and-remit system immediately, the Commission would provide some interim relief to providers suffering under the "historical data" approach of the existing USF system while allowing those providers sufficient time to prepare for the post-transition, connection-based USF system.

IV. The Commission Should Allow Carriers to Recover Administrative Costs of Collecting and Remitting USF Revenues

C&W agrees with other commenters that the Commission should continue to allow carriers to recover the administrative costs of collecting and remitting USF revenues.[29] The existing USF system permits such recoveries. And the billing and customer services costs under a connection-based USF system will likely be significant enough to justify such recoveries.

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[28] *See id.* at 13-15.

[29] *See, e.g.*, WorldCom FNPRM Comments at 9.

For non-dominant carriers, the Commission need not establish rules for recovery of collection- and remittance-related administrative costs. Competitive pressures would discourage any abuse. But in situations where abuse is likely, the Commission could establish a "safe harbor," such as a permissible recovery percentage reflecting average carrier administrative costs. Some commenters who are dominant providers of access lines seem comfortable with such an approach.[30]

[30] SBC FNPRM Comments at 13.

CONCLUSION

For the reasons set forth above and in its comments on the earlier NPRM, C&W urges the Commission to adopt a connection-based USF system, based on the CoSUS proposal, with a reasonable transition period.

Respectfully submitted,

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